PARTNERS FOR FINANCIAL STABILITY

Addressing Institutional Gaps in the Financial Sectors of the Baltic States, Central, Eastern and South-Eastern Europe

Conference Proceedings

June 8-9, 2000
Budapest, Hungary

Co-Sponsored by:

EAST • WEST
MANAGEMENT
INSTITUTE

USAID

PARTNERS FOR FINANCIAL STABILITY

Addressing Institutional Gaps in the Financial Sectors of the Baltic States, Central, Eastern and South-Eastern Europe

CONFERENCE PROCEEDINGS

OVERVIEW

On June 8-9, 2000, the East-West Management Institute ("EWMI") hosted a seminar on financial sector development in Central and Eastern Europe ("CEE") and Southeastern Europe ("SEE"). The seminar introduced the Partners for Financial Stability ("PFS") program, jointly funded by EWMI and the U.S. Agency for International Development ("USAID") to promote financial sector development in CEE and SEE countries, to 75 participants from 13 CEE/SEE countries. The CEE countries under the PFS program are defined as the USAID graduated or near graduated countries (Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, and Slovenia). The SEE countries under the PFS program are countries in Southeastern Europe with active USAID programs (Albania, Bosnia Herzegovina, Bulgaria, Croatia, Macedonia, Romania, Kosovo and Montenegro).

The seminar provided an opportunity for representatives of government, business, and non government organizations ("NGOs") from CEE and SEE countries to share with each other and representatives of donor organizations their experiences and concerns in the area of financial sector reforms. During the two-day seminar, four panels focused on banking, capital markets, insurance and pension reforms. Each panel was composed of experts in the specific discipline from CEE countries and Western Europe. The observations and comments of the seminar participants reflect the discussion between the panelists and participants regarding reforms in the four focus areas.

An excellent summary of the purpose of the PFS program, its goals and objectives was provided by **William Frej**, **former USAID Mission Director to Poland, and currently USAID Director of the Office of Market Transition, Bureau of Europe and Eurasia**.

> The theme of this conference is "partnership". Partnership is certainly an important concept that USAID has been advocating as one of our primary operating principles. In this regard the program on which we are here today is a program that we hope will help all of you better understand USAID's new Partners for Financial Stability Program.

PFS seeks to fill the gaps in the institutional development of financial sectors of graduated and soon to graduate Central and Eastern European countries

> PFS was initiated at the end of 1999 by USAID and it is a program that seeks to fill the gaps in the institutional development of financial sectors of graduated and soon to graduate Central and Eastern European countries in order to shorten the time required to meet international standards and accession to the European Union ("EU"). These countries include the Czech Republic, Estonia, Hungary, Latvia, Slovenia, Poland, Lithuania and the Slovak Republic. While it is appropriate for USAID to phase out of these countries, it is also premature to assume that the transition from a command to a market economy is

completed. These countries do not yet completely meet or practice international financial standards and this gap could certainly put at risk the significant reforms these countries have already accomplished.

The purpose of PFS is to address continued weakness in these Central and Eastern European financial systems. Such weaknesses could make the still fragile financial systems vulnerable to crisis, but continuing specialized technical assistance could help make key institutions more resilient and better able to deal with the threats of the transition process.

PFS consists of two components. The first component is focused on addressing gaps in the financial sectors of specific close out countries with assistance provided primarily by United States government agencies, such as the US Treasury and the US Securities and Exchange Commission. It also consists of assistance provided by private sector experts and contractors and as well NGOs such as the Financial Services Volunteer Corps that has been operating in this region from the very beginning of the transition in 1989.

Whereas this first component takes a bilateral approach, the second component of PFS, which is being implemented by the East-West Management Institute, is focused specifically on regional integration and regional linkages. The East-West Management Institute is implementing an inter-regional program of financial sector assistance. The program concept is to share ideas, lessons learned and policy recommendations and to build and strengthen inter-regional institutions to advance financial sector reforms in Central and Eastern Europe.

One way to encourage movement by CEE financial institution policy and decision makers is to adopt international standards creating and strengthening regional linkages and organizations including securities regulatory organizations, regional bank regulator organizations and private pension fund regulatory organizations, all of whom are represented here today. These regional organizations can share lessons learned and exchange information within the region and affiliate with international organizations.

The East-West Management Institute is also responsible for implementing an inter-regional or East-East technical assistance program drawing upon financial experts from the USAID graduated or almost graduated countries to provide advice in Southeastern European countries. Again, the concept is to share lessons learned and to provide training and institutional support, drawing upon the experience of USAID CEE graduated countries.

According to the panelists, each of the CEE countries has made progress in the area of financial sector reform. The conference participants also agreed that the progress toward reform, however, has been uneven across CEE countries in the areas of banking, capital markets, pension, and insurance.

The panel discussions highlighted some of the progress in CEE financial sector reforms, and areas where reform is still needed, as well as the areas where lessons learned from the CEE financial sector reform experience can be shared with SEE countries. SEE participants were quick to share the challenges facing them in these four financial sub-sectors and to outline areas where lessons learned from the CEE experience might be beneficial. The comments of the panelists and participants are highlighted below.

BANKING

CEE Perspective

The CEE experience in banking reform was discussed by **George Szapáry** on the first day of the conference, and by the Banking panel on the second day of the seminar. Mr. Szapáry, a senior advisor at the **National Bank of Hungary** and a former International Monetary Fund official, made a convincing argument based on Hungary's experience in bank privatization that one of the critical elements in the reform process is speed. He also explained that Hungary made an early decision to sell its banks to strategic investors, resulting in bank sales to foreign banks, as there was an insufficient number of strong domestic investors. In addition, he noted that countries still undergoing consolidation, should not provide government guarantees to strategic investors, but instead should sell the banks at a small discount. This recognizes that there may be bad loans that will turn up after the purchase. He described with great clarity some of the salient lessons learned about Hungary's bank privatization:

> Under [bank] consolidation, the longer the procedure the higher the expenses. I think this is not a typical Hungarian experience, as we have seen it everywhere else. But there are two reasons for that. One is that as banks consolidate the management and enterprises, they see that the state will bail out the bank, so those that can pay will just not pay or will just try to disappear from the scene. The banks also make less of an effort to collect because you need a lot of collecting, you incur a lot of expenses, and you need to sue the borrowers and so forth. Thus if you drag on the process of consolidation the cost will climb.
>
> The consolidation of the banking sector should be linked to enterprise restructuring. If the enterprises are not restructured or not yet privatized for instance, if they are still state-owned, and if you take away from the banks their bad loan portfolio, those enterprises will continue to generate bad loans to the extent that the banks are still willing to lend to them. So it has to be in tandem with the restructuring of the enterprises. Without strengthening financial disciplines in the corporate sphere, the banking sector rehabilitation cannot be successful.
>
> Finally, an important lesson we learned in Hungary is not to give government guarantees on bad or outstanding loans. When you privatize, the potential buyers sometimes spend a month or more sending as many as thirty people here to look at the banks. Then they say we found most of what we could find, but they are not one hundred percent sure whether they have found all the bad loans. So, they ask for a government guarantee. Three years after their purchase the owner comes back and says, listen, I found these bad loans and according to our agreement, you guaranteed that you would pay for these bad loans that originated before. And the government had to pay of course, but they got a lot of political criticism because it was very costly. So having gone through this, I would advise this: do not give a guarantee, rather sell the bank at a discount.

Without strengthening financial disciplines in the corporate sphere, the banking sector rehabilitation cannot be successful

Much of the shared experiences about banking reform by CEE participants and panelists also focused on issues of bank consolidation and privatization, strong supervision, and recapitalization following privatization. Panelists stressed the need to build strong information technology ("IT") systems and to leap frog to the next generation of electronic banking to rapidly reduce the costs associated with large branch bank networks. Consumer protection issues were also covered. Below is an overview of the lessons learned from the experience of several CEE countries, as described by **Roberto Rocha of the World Bank**:

> Stabilization and liberalization has been achieved in most of the region although it still remains an issue in some countries in Southeastern Europe. The entry of new banks has been achieved everywhere in varying degrees. With regard to restructuring and privatization of state banks, I think Poland and Hungary are the most advanced. Slovakia and

the Czech Republic are undergoing very deep reforms in this area right now. Slovenia achieved restructuring but is late with privatization. Many countries in Southeastern Europe are behind in these two areas and are still facing this issue. The workout of bad loans is another difficult area we have to face. Again Poland and Hungary did it before anybody else between 1992 and 1995 and have basically completed this task. The Czech Republic and Slovakia are doing it today and they are going through a very painful period of working out a huge amount of bad assets; Slovenia did a half-baked cake. Croatia is doing it now and most countries in Southeastern Europe face this problem, which is still to be resolved.

Banking regulation has been improved throughout the region, primarily with the objective of harmonizing legislation with the EU

Banking regulation has been improved throughout the region, primarily with the objective of harmonizing legislation with the EU; progress has been tediously slow. Legislation related to banking law, bankruptcy, foreclosure, and security lending has been very unsatisfactory in most of these countries. The Czech Republic and Slovakia are going through great efforts to improve their legislation, which is having noticeable results.

Unfortunately, bank regulation is an area where we do not have EU directives to guide us. There are no EU directives in the areas of bankruptcy and foreclosure. Europeans never could get an agreement on what kind of model they wanted. So there is more scope for individual choice in this area, but this is an area where a lot needs to be done. Not only bankruptcy, but also foreclosure and particularly enforcement and security lending in general.

Banking supervision is an area that remains a challenge all over the region. This is a developmental and an institutional problem. Some countries are meeting this challenge better than others, but this is an area, where even the most advanced countries have not reached the stage that is expected from OECD and EU new members. Technical assistance and bankruptcy legislation and procedures will remain on the agenda for donors for many years to come.

SEE Perspective

The banking privatization process of the CEE countries could be highly beneficial if transferred to the SEE countries. Banking crises have rocked Albania, and Bulgaria in recent years and many other SEE countries are undergoing deep banking reforms. The issues of banking privatization, improved supervision, training to develop commercial banking skills, consumer protection and an improved legal framework and enforcement are reform areas that may benefit from the CEE experience in bank reform. Two thoughtful comments from SEE participants were as follows:

Ivanka Petkova, **Executive Director, Economic Policy Institute, Sofia**:

In 1996-97 Bulgaria experienced one of the most severe banking crises which resulted in the closure of one third of the banks and costs equal to 14 % of GDP being incurred in resolving problems from the crises. Currently, the Bulgarian banking system is operating under a currency board arrangement. The currency board resulted in an extremely limited lender last resort option for banks in financial difficulty, which in turn resulted in bank liquidity and risk management issues. Also as a result of the crisis, more prudent regulations, stricter supervisory policy, higher requirements concerning bank solvency and elimination of self-credits and enforcement of hard budget constraints were adopted. Several possible measures could have positive effects on banking sector development. Among them are amendments to the legal framework, where the purpose should be the protection of creditor rights and training of bank staff to develop basic commercial banking skills, and monitoring and risk management policies and procedures that need to be adopted. These are all areas where we may benefit from the experience of Central European countries.

Albanian Delegate:
Allow me to briefly comment on banking reforms in Albania, including the main challenges and what should be done in the future. The legal framework for the banking sector in Albania has already been completed. The last two laws on money laundering and secured financing law were recently passed. Progress has been made in the establishment of the central bank and commercial banks. Still the Albanian economy is not responding to these reforms which include banking supervision, despite the work done by USAID, the Barents Group, Financial Service Volunteer Corps and so on, it remains one of the biggest challenges for establishing a better functioning banking sector in Albania. The most important continuing reform will be in the area of supervision. Also, training of bank staff in commercial banking skills is critical. Of course, public education and consumer protection continues to be a new challenge. The areas of better supervision, training of bank staff and consumer protection I think are the three most important banking reforms that need to be strengthened in Albania.

CAPITAL MARKETS

The discussion of capital markets development in CEE countries and the lessons to be learned in SEE countries was led by **Miroslaw Kachniewski, Secretary of the Polish Securities Commission** and Panel Chairman. He suggested four topics for discussion:

First, [there] is [the issue of] the relationship between privatization and the development of the capital market. The better capital market you have the easier it is to privatize and the more you privatize the larger capital market you have. We should also discuss the problem of mass privatization programs. Should mass privatization programs be developed and should these programs be linked to capital market development?

A second topic is what is the optimal level of regulation. Little or no regulation is not desirable but over regulation may retard market development. So what is the optimal level of regulation?

Third, should supervision be consolidated (that is banking, securities, pensions and insurance under one body) or would it be better to have several institutions that supervise particular parts of the market?

The fourth, is the issue of the integration of exchanges. This is directly linked to the question of integration in the European Union, and the question of meeting the requirements of the European Directives.

A lively discussion ensued on the topic of mass privatization and its role in the development of capital markets. Most participants agreed that mass privatization had serious shortcomings and that a lack of regulation compounded the development of capital markets particularly in the Czech Republic. **Mr. Jezek, a former Czech Minister of Privatization, now a Securities Commissioner in Prague** made the case that a lack of regulation of the market led to abuses and a lack of confidence in the market. Interestingly, however, **Marco Simoneti of CEEPAN** made an argument for a two track type of regulatory approach advocating strong regulation for blue chip public listings and for less strict regulation under the company law for voucher share holdings in many other companies. Some Polish delegates jumped in not only to state that the Czech mass privatization experience was completely flawed but also to take the panel's Chairman (Mr. Kachniewski from the Polish SEC) to task for the over regulation of the Polish market. A few of these interesting comments are as follows:

Tomas Jezek, Presidium, Czech Securities Commission:

I was [Czech] Minister of Privatization, and was personally responsible for mass privatization. Looking back today, I would still maintain that voucher privatization was the only solution possible at that time. Our mistake was failing to develop tighter [securities] supervision and regulation in the period after voucher privatization. We still had no IPOs [initial public offerings]. But I do not think that this is the outcome of voucher privatization itself, but the outcome of bad, non-existent regulation in the period after voucher privatization. In the mid-nineties we saw several financial scandals as a result of this failure to regulate. Since that time we have established the Czech Security Commission which was established almost exactly five years later than was necessary. There are many other problems we are working on such as disclosure, accounting standards, corporate governance, and trade reporting. I would say the lesson we learned was that tight securities regulation should have been introduced much earlier and this is what I would recommend to our colleagues from Southeastern Europe.

Our [the Czech Republic] mistake was failing to develop tighter [securities] supervision and regulation in the period after voucher privatization

Marco Simoneti, Executive Director, CEEPN, Slovenia:

In our countries we often have a set of laws that are not consistent because they were done through different aid schemes. Thus you have, for example laws based on an U.S. Securities law that conflicts or overlaps confusingly, with the German Company law. Then there is banking law which began with the American model used in Hungary but which then was switched to universal banking. Slovenia is now attempting to harmonize every law with those of the European Union. So, there is an opportunity to get a consistent set of laws that will instill investor confidence. So, maybe instead of listing every company then, why not have a separate, dual approach? Basic regulation and protection for shareholders could be provided through the company law. The regulations should be very strict western type rules for the companies that will be publicly traded on the stock exchange. For mass privatization companies the regulations could be from the corporate law. We would separate from those two thousand [mass privatization] companies the hundreds of potentially publicly listed companies. Then we could have very strict regulation for the publicly listed firms and more relaxed regulation for all of the others. I think this may be an approach that our colleagues [from Southeastern Europe] may want to examine as another approach to the question of regulation and the relationship between mass privatization and capital market development.

Basic regulation and protection for shareholders could be provided through the company law.

Finally, **Mr. Kachniewski** made a very good point about potential integration of capital markets across the region and the need for more standardized regulation as follows:

A comment on European regulations. This addresses the question of over-regulation and regulatory arbitrage on-going to various markets to find a place that is less regulated. European legislation gives us [the] possibility that the markets will be harmonized. At a minimal level it will mean a much greater degree of harmonization of laws throughout the region. I do not refer only to those countries that may be members of the European Union in the nearest future, but also to the others [in Southeastern Europe] because it's quite important to say to investors that we have already incorporated the provisions of EU directives concerning disclosure. It's a kind of standard. Thus, even those markets

[Southeastern Europe] that may not join the EU in the near future, could benefit from adopting EU standards.

In response to some of the discussion about the optimal level of regulation, **George Prohasky, Chairman of the Sofia Stock Exchange, Bulgaria** related the Bulgarian experience, which started with non-existent securities regulation and now has very strict regulation and related costs. His comments were as follows:

> I was just thinking that probably we [Bulgaria] really might be over regulated because, for example, even for a private placement you need to file a prospectus to the Security Exchange Commission in Bulgaria. Also, I would be interested to hear what other countries have adopted the concept of strictly regulated publicly traded company which has been incorporated in the legislation, because our latest law from last year especially treats the publicly traded company as a special type of company. And actually, if you are a publicly traded company, you register with the SEC and then you come on the different legislation, not the normal commercial code but you move to the securities law and there the criteria are much stricter for protection of minority shareholder rights…. So I don't know, maybe it's an interesting concept what Mr. Jerzek said, that the cost of regulation and the level of regulation are something different.
>
> The question is whether all other [countries] regulations is not that high, but as we have experienced all these pyramids and the failure of the unregulated trading in the first half of the nineties, we decided to go to the other extreme in a sense. And unfortunately, our trading is very low. But I don't think it is because of the lack of regulation. It's because of [a] number of other things. Primarily, because of the way the privatization was done here in Bulgaria. And, because none of the very big companies were privatized through public listings, which has been the case in Poland and in Hungary we failed to produce a market. So this question of the optimal level of regulation as well as the methods of privatization needs to be carefully considered.

An **Albanian Delegate** also agreed with Mr. Simoneti that a two-track approach to regulation may be worth exploring as an alternative to strict regulation for all companies. His comments were as follows:

> I wanted to [make] some comments. I would like to agree with Mr. Simoneti that maybe it's more sensible to adopt this dual approach because in transitional economies you could create two different markets. One would be with high standards for IPOs, for privatization's made by IPOs and with the name of other quite big companies to issue shares and to acquire capital. And this other segment would be connected somehow with mass privatization and dispersed ownership. And then you need market just for consolidation of control and you could adopt a more liberal approach to this segment.

INSURANCE & PENSION

To accommodate the interests of the seminar participants we merged the pension and insurance panels into one large panel discussion. The pension section of the panel was composed of an excellent mix of pension reform experts (**Roberto Rocha, World Bank, Juan Yermo, OECD, Dusan Kidric, Slovenia, and Tibor Parniczky, Chief Pension Regulator, Hungary**).

Pension reform has proceeded unevenly across the CEE countries. Some countries are quite advanced in implementing pension reforms that include the development of fully funded private pension programs while others are just beginning with basic legislation. Poland and Hungary are in the advanced group while the Czech and Slovak Republic are making good progress on the legal framework. Slovenia has Pillar I and II in place and is amending the law to implement Pillar III. The Baltic States are a mix, where some laws are in place and implementation has proceeded.

The discussion about pension reforms focused on some of the basic issues of design. The discussion also focused on regulatory issues and a model was suggested on unified regulation or regulation of banking, securities, pension and insurance under one institutional roof rather than separate institutional bodies. Hungary currently has a unified regulatory body. In addition some interesting discussion about the role of pension funds in the development of the capital market and the limits of good assets for these funds to invest in was touched upon by several participants.

The discussion on insurance benefited from a mix of practitioners (**Kalman Mizsei, AIG Insurance, David Lewis, Chief Actuary of the Government Actuary's Department in London**) and experts (**Cecile Vignial, OECD**) and a regulator (**Laszlo Asztalos, Insurance Regulator, Hungary**). Much of the discussion centered on developing best practices for insurance, consumer protection and better regulation.

Cecile Vignial of the OECD outlined some of the key obstacles facing Central and Eastern Europe in the development of insurance markets while outlining OECD principles for addressing the lack of regulation and liberalization of insurance markets in the region. Briefly her comments were as follows:

> I would like to address the obstacles to the development of the insurance market. First, Central and Eastern Europe lacks an insurance culture. Another obstacle is mistrust of financial institutions. Previously insurance was seen more as a tax and today its role is often still not well understood. Another obstacle is a lack of know-how. I want to focus on the way OECD tackles the issue of insurance market development and the issue of regulation.
>
> To assist countries to upgrade their regulations, the OECD has developed a lot of technical assistance, policy dialogue, many studies, and also some guidelines. Some of these guidelines include: The need for very strict licensing procedure to protect consumers from failures. The second principle is the development of compulsory insurance like motor vehicle liability insurance. A third principle is the development of appropriate contract law that is so important for the trust of consumers. A fourth principle is to define the taxation of insurance products. The last principle is the need to develop private pension reform in an appropriate regulatory framework. This is a great booster for life insurance markets. This region will always be of great importance for the OECD and we are ready to launch other kinds of further cooperation especially through the East-West Management Institute.

A **Delegate from the Ministry of Finance of Macedonia** posed three questions to Laszlo Asztalos, former Chief of Insurance Regulation of Hungary. Her questions were as follows:

> My first question is about the EU directives for insurance. You stated that you started with the insurance reform in Hungary fourteen years ago and that you have started with the negotiation for association with the EU in the early nineties. Can you tell us how compliant are your regulations with EU directives and how advantageous or disadvantageous it is for full accession of Hungary into the EU?
>
> Secondly, what about the incentives you give to foreign investors and to foreign insurance companies to invest in the insurance industry? This is very important for the Republic of Macedonia currently.
>
> Thirdly, can you explain a little bit more about the supervisory function in Hungary, how it is organized in Hungary, especially the onsite examinations, from the point of view and in terms of the establishment of the body and the hiring of staff, training of staff, computer and so on?

Mr. Asztalos answered the questions in detail and the PFS program subsequently received a request for assistance from the Macedonian Ministry of Finance to learn more about Hungarian insurance regulation experience.

In the area of pension reform several perspectives were discussed about the design of pension systems as well as the regulation of pensions and the problems encountered by pension funds seeking to invest in good domestic assets. A few of the more interesting comments are highlighted below:

Roberto Rocha, World Bank:

Full three pillar systems have been passed and are being implemented in Hungary and Poland, which are the two pioneers. Full three pillar systems have been passed and are to be implemented in Croatia, Latvia and Macedonia. First and third pillar systems without a second pillar, a mandatory pillar have been passed and are going to be implemented in Slovenia; they exist already in the Czech Republic. And multi-pillar systems are under elaboration or discussion and consideration in a number of other countries in the region as well, such as Romania and Slovakia. The legal structure of the systems that we see today involving the regions is not the same. There are variations from country to country. The supervision agencies are young, they need to learn their work better, a capacity has to be built up. There is also always the question of whether supervision should be alone or integrated. There is a movement, I would not say there is a trend in the world, but there are more and more countries [that] are integrating their supervisions. Whether this is good or bad, I think the jury is still out.

Marek Gora, Poland:

In Poland our decision was to focus on income allocation. Having the system focus on income allocation creates clear incentives for the people to participate in the system. You pay the money in, money brings profits and eventually you get the money back plus interest. This is why we decided to have as large a volume as possible with investments in stocks or financial instruments other than government bonds. We also terminated the whole [old] system. There is no switching in the Polish system. You cannot switch from the old to the new. The old does not exist any more for people born after 1948. So for the older people no reform at all; for younger people, below fifty it is a very deep reform.

Tibor Parniczky, Chief Pension Advisor, Hungary:

We implemented our pension system two years ago and the final stage in the legislation was that merger of the supervisions of capital market banking, insurance and pensions in Hungary. This will give, higher standards to pension funds because they will be compared to banks, investment funds and other financial institutions in one building. We regard it as a challenge or an opportunity to improve the capacities of the Hungarian pension funds. The mandatory pension funds, could not invest abroad in 1998. Now they can invest 10% of their assets abroad. What we found during the 1998 stock exchange crisis in Hungary was that it was a good test. The pension funds of basically conservative investors and over 75% of their investment is in Hungarian government bonds and the minor part to stocks and investment funds. What we found in 1998 was that the new money which went into the pension funds, again, they did not buy stocks but rather it was invested it again in government bonds or investment funds. So for that period the ratio of government bonds and other types of investment were higher than for stocks.

CONCLUSION

In summary, EWMI found that the conference facilitated a sound exchange of ideas between the CEE experts, donors and OECD experts on the panels and the participants from the CEE and SEE countries. In some cases, participants found common ground on issues such as banking privatization or the optimal level of regulation for banking, securities, pensions and insurance. In other cases participants voiced disagreement on whether mass privatization worked at all, and whether it did more harm than good to the development of capital markets. To some extent the issue is moot except in Bosnia Herzegovina and a few places where mass privatization programs may still be implemented.

Overall, it is clear that European Union accession is a powerful motivator for greater regional standardization of all four financial sub sectors. In order to speed up the EU accession process, the less developed countries in the group would like to avoid some of the EU accession problems encountered by their neighbors, and benefit from the lessons learned by the more developed countries. In the areas where the process of privatization is less developed, namely in pension and insurance reform, there is a desire to adopt a more collective approach to these shared social issues. The discussion also indicated that the majority of countries require assistance in implementing best practice methodologies across the four sector areas addressed during the conference.

A clear message resulting from the conference was that opportunities for regional cooperation in financial sector reform will continue throughout the decade. It is the objective of PFS to turn these opportunities into effective reform in the four sectors. Also, the seminar reinforced the perception that experts from CEE countries seek to share the lessons learned of their financial sector reforms with counterparts in SEE countries who are beginning to develop and implement some of these same reforms.

EWMI's PFS team has used this conference as a springboard to develop projects, sub-grants and regional associations in order to attempt to address some of the needs revealed during the conference. EWMI has contacted the speakers and participants from the conference to follow up on the issues discussed, and to ascertain how PFS can work with them to address these issues. In addition to the positive responses from many individuals, there were a number of suggestions that have evolved into projects, such as the development of a joint project with OECD to create a pension reform network in CEE. EWMI looks forward to continuing this ongoing exchange of information with counterparts in the region to address the institutional gaps in the financial sectors of CEE and SEE countries, and to develop sub-grants, joint projects and other activities.

FOR FURTHER INFORMATION ON PFS, PLEASE CONTACT:

Richard Guilford
East-West Management Institute - Hungary
Karoly korut 11
Europa Center
Budapest, Hungary 1075
Tel. (36-1) 269-7888
Fax. (36-1) 267-3547

CONFERENCE AGENDA

Thursday: June 8, 2000

Welcoming Address
Richard Guilford, Director
Partners for Financial Stability Program
East-West Management Institute, Inc.

The PFS Program: Introductory Remarks
William Frej, Mission Director
U. S. Agency for International Development, Poland
Director (Designate), Office of Privatization and Economic Restructuring, Europe and Eurasia Bureau, USAID, Washington, D.C.

Financial Sector Reform: Hungary's Experience
Gyorgy Szapary, Advisor to the President, National Bank of Hungary

Friday: June 9, 2000

Panel I - Capital Markets:
What further reforms are required in the development and regulation of these markets? What is the impact of globalization and European Union accession on the CEE/SEE/Baltic markets and the prospects for integration of these markets? How can the PFS program assist in these reforms?

Panel Speakers:
Chairman: Miroslaw Kachniewski, Secretary of the Securities and Exchange Commission, Warsaw
Marko Simoneti, Executive Director, Central Eastern European Privatization Network, Ljubljana
Tomas Jezek, Member of the Presidium, Czech Securities Commission, Prague
Dr. Frigyes Harshegyi, Former Deputy President (International) Hungarian National Bank, Budapest

Panel II - Banking:
What further measures should be taken to assist banking sector reform? How can the PFS program assist in these reforms?

Panel Speakers:
Chairman: Stefan Kawalec, Chief Advisor to the Board, Bank Handlowy w Warszawie S.A., Warsaw
Jan Jansta, Executive Director, Bank relations, Deloitte & Touche, Bratislava
Charles Kovacs, Senior Advisor, Arthur Anderson, Budapest
Roberto Rocha, World Bank, Lead Economist, Budapest

Panel III - Pension Reform:
What are the preconditions for the development of private pension funds and international standards in CEE countries? How can the PFS program assist in these reforms?

Panel Speakers:
Chairman: Prof. Marek Gora, Warsaw
Dusan Kidric, Head of the Department for Social Analysis and Development, Institute of Macroeconomic Analysis and Development, Ljubljana
Tibor Parniczky, Chief Pension Advisor, Hungarian Financial Services Authority, Budapest
Roberto Rocha, World Bank, Lead Economist, Budapest

Panel IV - Insurance:
What are the obstacles preventing the CEE countries from developing their insurance markets? How can the PFS program assist in these reforms?

Panel Speakers:
Chairman: Kalman Mizsei, Budapest
Laszlo Asztalos, Chief Advisor, Tolerancia Consulting Ltd., Budapest
David Lewis, Chief Actuary, Government's Actuary Department, London
Cecile Vignial, Organization for Economic Co-operation and Development, Paris

Presentation on EU Integration process and Accession Related Actions
David Daly, Delegation of the European Commission, Budapest

Review Panel
Chairman: Brian Hannon, Manager of Program Development, East-West Management Institute
All Panel Chairmen (Messrs. Kachniewski, Gora, Miszei, and Kawalec) and Mr. Guilford

Closing Remarks
Richard Guilford, Director
Partners for Financial Stability Program,
East-West Management Institute, Inc.

SPEAKER'S BIOGRAPHIES

Richard Guilford, *Director, PFS Program, East-West Management Institute, Inc.*
Mr. Guilford directs the EWMI PFS program. Prior to joining EWMI, Mr. Guilford managed financial sector and other reform projects for the European Commission in Budapest since the early 1990's. He is an investment banker with many years of experience developing and managing sovereign and private sector business in Latin America, Europe and the Middle East for leading international investment banks. He holds masters degrees in European Union Law (Leicester) and Business Administration (INSEAD).

William Frej, *Mission Director, United States Agency for International Development* ("USAID"), *Warsaw, Poland and Director (Designate), Office of Privatization and Economic Restructuring, Europe and Eurasia Bureau, USAID, Washington, D.C.*
Since 1997, Mr. Frej has served as Poland's USAID Mission Director, managing a $1 billion program, primarily focusing on strengthening local governments, and the further development of competitive, market-oriented financial and private sectors. Prior to that position, Mr. Frej had been Director of Regional Housing and Urban Development Office for Central and Eastern Europe for USAID, and served in the same capacity in USAID offices for Indonesia and the Philippines. In September 2000, Poland will graduate from USAID assistance and Mr. Frej will become Director of the Office of Privatization and Economic Restructuring, Europe and Eurasia Bureau in Washington, D.C.

Gyorgy Szapary, *Advisor to the President, National Bank of Hungary*
Mr. Szapary has served as Advisor to the President of the National Bank of Hungary since 1999. Prior to that time, Mr. Szapary spent six years as Deputy President of that institution. He has been the International Monetary Fund's ("IMF") Senior Resident Representative in Hungary and worked at the IMF in Washington, D.C. for 24 years, where his final position was Assistant Director of the Asian Department.

David Daly, *Delegation of the European Commission ("EC"), Budapest*
Mr. Daly has been the head of the Political and Economic Unit of the EC Delegation in Budapest since 1996. Prior to his current position, he was a European Union trade negotiator to the European Agreements with Central and Eastern European Countries. He has also been an auditor at the European Agriculture Guidance and Guarantee Fund in the Directorate General for Agriculture in Brussels. In addition, he was an Executive Officer in the Irish Department of Agriculture and also served in the Irish Department of Foreign Affairs. He holds a masters degree in economics from Trinity College and a bachelors degree in public administration also from the University of Dublin.

CAPITAL MARKETS PANEL

Chairman:
Miroslaw Kachniewski, *Secretary of the Securities and Exchange Commission, Warsaw*
Mr. Kachniewski has served as Secretary of the Polish Securities Commission since January 1, 1999. In addition, since 1995, he has been conducting research on financial markets at the Warsaw School of Economics International Finance Department. Mr. Kachniewski also serves as Chairman of the Working Group on Enforcement and Exchange of Information of the Emerging Markets Committee of the International Organization of Securities Commissions. Previously, he had been the Deputy Secretary of the Polish Securities Commission and a counselor at the Ministry of Privatization. He holds a Ph.D in economics from the Warsaw School of Economics.

Panel Members:
Marko Simoneti, *Executive Director, Central Eastern European Privatization Network (CEEPN), Ljubljana*
Mr. Simoneti, who holds a Ph.D in economics from Cornell University, currently teaches courses on financial institutions and corporate finance at the University of Ljubljana, and acts as Executive Director of CEEPN. CEEPN was founded by Central and Eastern European countries to support economic transition in the region by providing channels for sharing experience, knowledge, and skills between the experts and institutions of various countries. Mr. Simoneti has experience in all areas of economic reform in transition economies, with a particular emphasis on bank sector restructuring, financial reform, small and medium enterprises and privatization issues.

Tomas Jezek, *Member of the Presidium, Czech Securities Commission, Prague*
Mr. Jezek is an economist with years of economic reform experience in the region. Having been involved in economic reform since 1964, Mr. Jezek has a unique perspective on reform both prior to and throughout the transition period. From 1990 to 1992, Mr. Jezek served as Minister of Privatization of the Czech and Slovak Federal Republic. Between 1992-94, he served as Chairman of the Czech Fund for National Property and as a Member of Parliament and Chairman of the Budget Committee. Between 1996-98, Mr. Jezek was Chairman of the Prague Stock Exchange. Since 1998 he has been a Member of the Presidium, Czech Securities Commission, as well as serving on numerous boards

and committees. He has also served as an advisor on privatization and capital markets development and regulation in Bosnia, Kazakhstan, Russia, Ukraine.

Dr. Frigyes Harshegyi, *Former Deputy President (International) Hungarian National Bank, Budapest*
As the Deputy President of the National Bank of Hungary from 1990 to 1997, Dr. Harshegyi was responsible for the country's foreign debt and foreign exchange reserves management. He was appointed as Chairman and Chief Executive Officer of CIB Securities, Ltd., Budapest in 1999 and was previously a Member of the Board of Central European International Bank Ltd., where he was Deputy Chief Executive Officer and General Manager of Capital Markets. Mr. Harshegyi holds a Ph.D in Law from the University of Szeged.

BANKING PANEL

Chairman:

Stefan Kawalec, *Chief Advisor to the Board, Bank Handlowy w Warszawie S.A., Warsaw*
Mr. Stefan Kawalec has served as Chief Advisor to the Board at Bank Handlowy w Warszawie S.A., since 1994. Prior to joining Bank Handlowy, Mr. Kawalec worked in the Polish Ministry of Finance as Director General-Chief Advisor to Deputy Prime Minister and Minister of Finance and Undersecretary of State. In addition, Mr. Kawalec served as the Chairman of the Supervisory Board of Bank Pekao, S.A., Deputy Governor in the Board of Governors for the European Bank for Reconstruction and Development and Chairman of Interministerial Task Force on Debt for Environment Conversion of Polish External Debt. Mr. Kawalec has provided consultancy services on banking and transition issues in numerous countries including Latvia, Ukraine and Bosnia.

Panel Members:

Jan Jansta, *Executive Director, Bank Relations, Deloitte & Touche, Bratislava*
Prior to becoming the Executive Director of Bank Relations at Deloitte and Touche, Mr. Jansta was the Senior Executive Vice-President and Vice-Chairman of the Board of Directors of the VUB, A.S., the largest financial institution in the Slovak Republic. Previously, he worked as Head of the International Department at both the Ministry of Finance and the Office of the Prime Minister. In addition, Mr. Jansta spent 18 years as the Head of Trade Finance and Foreign Exchange Department for the State Bank of Czechoslovakia in Bratislava.

Charles Kovacs, *Senior Advisor, Arthur Anderson, Budapest*
Mr. Kovacs currently acts as an Advisor to a number of organizations, including Arthur Andersen & Co, Kft. and British Airways/Speedwing in Hungary and Elliott Associates, L.P. in New York. Additionally, he serves on the Supervisory Board of Radio Bridge, LLC. Mr. Kovacs has been Director and Head of the Budapest office of the Barclays Bank Group and Director of Corporate Finance for Price Waterhouse. Prior to these positions, he spent almost twenty years working internationally for Chase Manhattan Bank where he was last Vice President and Manager of International Programs.

Roberto Rocha, *World Bank, Lead Economist, Budapest*
Mr. Rocha has worked at the World Bank for fifteen years, spending the last seven years as Lead Economist in the Regional Office in Budapest. While in the Budapest office, Mr. Rocha's primary responsibilities have been the following: banking and capital market reform, enterprise reform, pension reform and macroeconomic assessment. In his work covering Hungary, Czech Republic, Slovak Republic and Slovenia, Mr. Rocha has published numerous articles and papers on financial sector issues in these countries.

PENSION REFORM PANEL

Chairman:

Prof. Marek Gora, *Warsaw*
Professor Gora has been involved in the pension area for over twenty years. After receiving his Ph.D from Warsaw School of Economics in the early 1980s, he has continued to conduct research and lecture there. In addition, he was instrumental in the design of the pension reform program, *Security through Diversity*, which the Polish government began implementing in January, 1999. In addition to his work in Poland, Professor Gora has provided pension reform advice in Macedonia and the Slovak Republic. He has also worked with the Directorate for Education Labor and Social Affairs at the OECD and is currently a Research Fellow at the William Davidson Institute at the University of Michigan.

Panel Members:

Dusan Kidric, *Head of Department for Social Analysis and Development, Institute of Macroeconomic Analysis and Development, Ljubljana*
In addition to his current position as Head of the Department for Social Analysis and Development, Mr. Kidric serves as an advisor to the government, a member of the Social Economic Council of the Republic of Slovenia, and as a member of the Expert Board of the Agency for Insurance Supervision. His expertise lies in social development and social security, as well as social insurance and public financing. With such varied expertise in these areas, Mr. Kidric has served as an advisor on several projects in Slovenia and provided papers for numerous conferences.

Tibor Parniczky, *Chief Pension Advisor, Hungarian Financial Services Authority, Budapest*
Mr. Parniczky, who holds a university degree in software design and mathematics, has worked in the pension field since 1989. After serving as senior expert for Human Risk Management, Ltd., Mr. Parniczky became an Advisor to the Ministry of Finance and shortly thereafter, began his tenure as Vice President to the State Private Funds Supervision of Hungary. Currently, Mr. Parniczky serves as Chief Pension Supervisory Counselor of the newly established integrated Financial Supervisory Authority of Hungary. As one of the architects of the new system, Mr. Parniczky is a frequent speaker at conferences and training programs concerning pension reform in the region.

Roberto Rocha, *World Bank, Lead Economist, Budapest*
[See Banking Panel above]

INSURANCE PANEL

Chairman:

Kalman Mizsei, *Chief Investment Officer for Central and Eastern Europe, AIG Global Investment Corporation, Budapest*
As Chief Investment Officer for Central and Eastern Europe for AIG Global Investment Corporation since 1997, Mr. Kalman Mizsei, among his many other responsibilities, oversees the management of AIG's insurance portfolios in Central and Eastern Europe and serves as a member of the Supervisory Board of AIG's Polish pension fund management company. Prior to taking his position at AIG, Mr. Mizsei served for two years as Chairman of the Hungarian Export Import Bank Ltd. and Hungarian Export Credit Insurance Ltd. In addition, Mr. Mizsei was Vice-President for Economic Programs for the Institute for East West Studies in New York, and served as a Board Member of Budapest Bank and Advisor to the President of the National Bank of Hungary.

Panel Members:

Laszlo Asztalos, *Chief Advisor, Tolerancia Consulting Ltd., Budapest*
As Chief Advisor of the Tolerancia Consulting Ltd. since 1990, Mr. Laszlo Asztalos has extensive experience working in insurance development. He served as the President of the Hungarian State Supervisory Authority of Insurance from 1992-2000. Mr. Asztalos has also served as Director at the Managing Research Institute and Head of the Department of Fiscal Policy, both of the Ministry of Finance.

David Lewis, *Chief Actuary, Social Security, Government Actuary's Department, London*
In his role as Chief Actuary in Social Security at the United Kingdom's Government Actuary Department, Mr. Lewis provides advice to Ministers and officials at the Department of Social Security and other government departments on the benefits and finances of the National Insurance Fund. In addition, he has provided advice on private pension funds in transition countries, such as Latvia and Lithuania. Prior to taking his position as Chief Actuary, he served three years as an actuary in life insurance supervision. Previously, Mr. Lewis was an examiner for the Institute of Actuaries and Chairman of the Joint Board of Examiners of the Institute and Faculty of Actuaries.

Cecile Vignial, *Organization for Economic Co-operation and Development, Paris*
Ms. Vignial is Administrator in the Insurance and Private Pensions Unit of the Directorate for Financial, Fiscal and Enterprise Affairs of the OECD. She is in charge of the activities of the OECD Insurance Committee with non-member countries. In her role as Administrator of the Insurance Committee, Ms. Vignial's primary duty is to manage the technical assistance and policy dialogue provided to non-members by the Organization in the insurance and private pension area. Her research focuses are regulatory policy issues, and the promotion of related best practices. Ms. Vignial has worked for 8 years at the OECD. She graduated in economics at the Institut d'Etudes Politiques de Paris and has a MSc in Economics from the London School of Economics.

REVIEW PANEL

Brian Hannon, *East-West Management Institute, Inc. New York*
Mr. Hannon is Manager of Program Development for the East-West Management Institute, Inc. Prior to joining EWMI, Mr. Hannon was a principal in charge of Booz-Allen & Hamilton's privatization practice for Central and Eastern Europe (CEE) and the New Independent States (NIS) of the former Soviet Union. Between 1991-92 he was Director for CEE/NIS at the Center for International Private Enterprise of the U.S. Chamber of Commerce. From 1988-91 Mr. Hannon was Special Assistant to the Administrator of the U.S. Agency for International Development. He also held trade policy and investment positions respectively with the U.S. Department of Commerce and the Overseas Private Investment Corporation.

ORGANIZER

EAST-WEST MANAGEMENT INSTITUTE

East-West Management Institute, Inc. (EWMI) is a not-for-profit organization dedicated to promoting economic reform in developing and transition economies. EWMI assists countries in making their transition from planned to free market economies by providing technical assistance in such areas as legal and regulatory reform, privatization, enterprise restructuring, capital markets development, and making grants to non-governmental organizations (NGOs).

Founded in 1988 by financier and philanthropist George Soros to assist legal and economic reform in Central and Eastern Europe and the Soviet Union, EWMI has become an internationally recognized, multi-million dollar organization. EWMI manages hundreds of highly skilled international and local consultants who design state-of-the-art economic reform programs, draft and implement laws, develop accounting standards, privatize collective farms, and train government officials and judges.

Since the fall of the Berlin Wall in 1989, the countries of Central and Eastern Europe and the Newly Independent States of the former Soviet Union (CEE/NIS) have been striving to achieve sustainable private sector economic growth, which is possible only in an environment of market oriented institutions and policies, and transparent commercial laws and regulations. To establish such an environment, many countries have undertaken ambitious programs of privatization, legal reform, enterprise restructuring, and other economic initiatives.

EWMI assists these efforts by working with government officials, private sector companies, NGOs and individual citizens, targeting areas including commercial law reform, financial sector legal and regulatory reform, accounting reform, judicial training, and capacity building programs for privatization, enterprise restructuring and capital markets development.

EWMI offers expert services to meet the needs of emerging markets, and is dedicated to providing innovative solutions to the challenges of developing economies. EWMI recognizes that market-oriented reforms and policies are possible only with strong local leadership and political support, and EWMI's success in many countries is directly linked to its close collaboration with leading reformers.

The Early Years

During its first five years, EWMI arranged internships for professionals from CEE/NIS countries in Western Europe and the United States. Beginning in 1992, EWMI developed Junior Achievement (JA) programs and introduced them throughout CEE/NIS middle schools and high schools. In 1993, working closely with Junior Achievement International, EWMI launched the Fundamentals of Market Economy (FOME) program. This "senior achievement" program educated adults throughout the region in the basics of a market economy.

In 1993, EWMI expanded into local training activities by organizing a series of three- to six-month accounting training courses in the Baltic countries, Russia, Ukraine, and Moldova. Overseen by Professor Adolf Enthoven of the University of Texas at Dallas, these courses successfully trained over 10,000 accountants in the basics of Western accounting principles.

Current Activities

In 1995, EWMI was one of a select group of firms to be awarded a multi-year, multi-million dollar "Omnibus Contract" from the United States Agency for International Development (USAID) to provide technical assistance to reform efforts in the CEE/NIS. The first EWMI project under this contract was launched in October 1995. Since that time, EWMI has assembled hundreds of international and local professionals to plan and implement programs, including: Enterprise Restructuring in Hungary and Moldova, Land Reform and Privatization in Moldova, Accounting Reform in Moldova, Legal and Regulatory Reform in Bosnia Herzegovina, Judicial Training in Albania and Judicial Reform in Bulgaria.

The following are just a few of EWMI's achievements under these projects to date:

- The privatization of over 700 collective farms in Moldova, resulting in over 2,000,000 individual land titles being issued to new private farmers.
- The adoption of international accounting and auditing standards by the Republic of Moldova and the Federation of Bosnia Herzegovina, and the implementation of these new standards by private enterprises.
- The establishment of Securities and Exchange Commissions and the drafting and adoption of corporate and securities legislation by the Federation of Bosnia Herzegovina and Republika Srpska.

EWMI compliments its USAID-funded consulting activities with its own programs and grants to local organizations. For example, EWMI manages an extensive USAID legal and regulatory reform project in Bosnia that is responsible for drafting and implementing many commercial and capital markets laws. EWMI supports this effort through grants to the Law Center at the University of Sarajevo Law School for commercial law training and the maintenance of a commercial law database and website.